

## HC: Guarantee charges not interest, taxable under Article 23(3) as accrued in India; Distinguishes Capgemini

May 29, 2024

Johnson Matthey Public Limited [TS-365-HC-2024(DEL)]

### Conclusion

Delhi HC dismisses Assessee's appeals and holds that guarantee charges received by it from the Indian subsidiaries for guaranteed repayment of debts owed to third parties by the said subsidiaries accrued in India and hence, is taxable in India as per Article 23(3) of India-UK DTAA (DTAA); Holds that as Assessee had not extended any credit or lent capital to its Indian subsidiaries, the guarantee charges do not qualify as "interest" under Article 12(5) of the DTAA; In the present case, Johnson Matthey Public Limited Company (the Assessee), is a tax resident of UK; During the impugned AY 2011-12, it received guarantee charges aggregating to Rs. 1.49 Cr. from those subsidiaries for guarantee provided in respect of credit facilities extended by banks to its Indian subsidiaries in terms of the "Intra Group Parental Guarantee and Counter Indemnity Services Agreement" entered into with them; Refers to the SC judgments in [E.D. Sassoon](#) and [Seth Pushalal Mansinghka](#) wherein the expressions "arise" or "accrue" as referred in Section 5 were interpreted to mean a periodical monetary return being received with some regularity and that accrual of income is not dependent upon actual receipt and the moment a right to receive came into existence, income would be deemed to have arisen or accrued; Refers to the Allahabad HC judgment in [M.K. Brothers](#) (affirmed by SC) where this principle is explained; Holds that the income in the form of guarantee charges had in fact accrued and arisen in India and that *"the guarantee charges clearly answered to the description of income accruing and which was explained by the Supreme Court to constitute "a periodical monetary return "coming in "with some sort of regularity, or expected regularity, from definite sources"*; Observes that it is evident from the Intra Group Agreement which is the foundational source of those payments that the obligation to pay guarantee charges was incurred in India, was in respect of services utilized in India and was agreed to arise with regularity as per the stipulations forming part of the Intra Group Agreement; Observes that in case of default by Indian subsidiaries, the lenders could have recourse against the assets of the Assessee situated overseas and that guarantee charges may be utilized by the Assessee to meet its liabilities to overseas financial institutions is wholly irrelevant to determine whether income had arisen or accrued in India; Relies upon the SC judgment in [Tuticorin Alkali](#) wherein it was held that the Act is not concerned with destination or utilization and it is focused on the aspect of income having arisen or accrued; Holds that the source and fountainhead of the receipt was thus indelibly connected and confined to the Intra Group Agreement and the obligations of the Assessee in connection therewith and consequently the right to receive was also based on that agreement.; Distinguishes Mumbai ITAT ruling in [Capgemini](#) on the grounds that (i) Ruling proceeded on a mere ipse dixit that "from the record" the guarantee commission did not accrue or arise in India, (ii) ITAT took the position that since the guarantee was given by a French Assessee to a bank situate in that country, income could not be said to have arisen or accrued in India, (iii) in the present case, the guarantee charges were not founded on any contract that the Assessee may have had with a foreign bank but sourced and indelibly tied to the Intra Group Agreement; HC observes that guarantee charges were received by the Assessee neither in respect of any debt owed to it by its Indian subsidiary nor is it income derived from claims that the Assessee may have had against its Indian subsidiaries; Upholds the ITAT's finding that the Assessee was neither a party to the loan agreements that may have been executed nor was there any privity of contract that could be said to exist and hence, the guarantee charges that the Assessee received was a remuneration for the assurance that it had offered and that the debt that it owed was to those lenders who extended credit facilities to subsidiaries which could have a claim against the Assessee; Hence, holds that guarantee charges are not income derived from a debt or a claim and do not qualify as "interest" under Article 12(5) of the DTAA and also, under Section 2(28A) of the Act; Takes note of the coordinate bench ruling in [Lease Plan](#) wherein it was held that *"in absence of provision of capital and any debt claim between the parties the impugned guarantee fees paid by the Assessee to the Netherlands based company cannot be held to be "interest" in terms of Article 11 of the DTAA."*; Distinguishes United States Court of Appeals judgment in Container Corporation; Thus, dismisses Assessee's appeals; Refuses to decide the issue of whether guarantee charges would constitute business

income and fall within the ken of Article 7 of the DTAA as no question was formulated with regard to the same and keeps the said question open to be addressed in an appropriate case;:HC DEL

### Decision Summary

The judgment was delivered by the Division Bench of the Delhi High Court comprising Justice Yashwant Varma and Justice Purushendra Kumar Kaurav.

Senior Advocate Percy Pardiwalla along with Advocate Prakash Kumar appeared for the Assessee while the Revenue was represented by Senior Standing Counsel Abhishek Maratha along with Junior Standing Counsel Parth Semwal and Advocate Nupur Sharma

The Assessee, a tax resident of UK, is engaged in the manufacture of specialty chemicals and it has also established various subsidiaries across the globe including in India. During the impugned AY 2011-12, the Assessee extended guarantees to various overseas branches of foreign banks on a global basis in relation to credit facilities extended by those financial institutions to its Indian subsidiaries, namely, Johnson Matthey India Private Limited and Johnson Matthey Chemicals India Private Limited. In connection therewith, the Assessee and its various Indian subsidiaries executed the Intra Group Parental Guarantee and Indemnity Services Agreement in March 2010. In lieu of the guarantee that it provided to banks and financial institutions who extended credit facilities to its subsidiaries in India, it received guarantee charges aggregating to Rs. 1.49 Cr. from those subsidiaries. The Assessee filed return for the impugned AY characterizing the amount of guarantee fee as interest falling under Article 12 of the India-UK DTAA. The Revenue passed the draft assessment order, taxing the guarantee charges under Article 23(3) as "other income". The DRP confirmed the same. The Assessee filed an appeal before the ITAT which was dismissed. The present appeal is filed by the Assessee before the HC.

### Case Law Information

#### Taxpayer Name

- Johnson Matthey Public Limited

#### Judicial Level & Location

- High Court Delhi

#### Appeal Number

- ITA 727/2018

#### Date of Ruling

- 2024-05-28

#### Ruling in favour of

- Revenue

#### Section Reference Number

- 2(28A)
- Articles 12 and 23 of India-UK DTAA

#### Nature of Issue

- interest

#### Judges

- Justice Yashwant Varma

- Justice Purushaindra Kumar Kaurav

**Counsel for Tax Payer**

- Mr Percy J. Pardiwalla
- Prakash Kumar

**Counsel for Department**

- Mr Abhishek Maratha
- Mr. Parth Semwal
- Nupur Sharma